



March 25, 2009

Ms. Mary F. Rupp
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428

Dear Members of the Board:

We appreciate the opportunity to provide comment on NCUA's advance notice of proposed rulemaking for 12 CFR Part 704 and request for comment on corporate credit unions.

Corporate Credit Unions are as intricately woven into the credit union system as natural person credit unions. They are an important provider of vital services especially to small and mid-sized credit unions. The financial environment we find ourselves in today has transcended all phases of the credit union system. We appreciate the opportunity NCUA has given in allowing natural person credit unions to respond to the operational and regulatory structure of the corporate system. We will address each component of the restructuring for which NCUA has solicited comment.

The Role of Corporates in the Credit Union System

Payment Systems

Currently, all components of the corporate credit union system are coupled together under one umbrella, and you ask the following questions:

- 1) Should payment services be isolated from other services to separate the risks? If so, how is this best achieved?
 - Payment systems are but one component of the corporate system on which we so heavily depend. I do not believe that isolation is a viable solution in and of itself. In addition, to payment systems, natural person credit unions lean heavily on our corporates for liquidity and deposit needs, wire and western union transfer services, settlement services for ATM, ACH, and Debit payments, check imaging and retrieval, and Check 21 services. I do believe that these components could be sheltered as a wholly owned subsidiary of each corporate, thereby isolating that portion of the system from the volatility of market conditions.
- 2) Would it be better to establish a charter for corporates whereby a corporates authority is strictly limited to operating a payment system, with no authority to engage in other services, such as term or structured investments?
 - The corporates must have the flexibility to engage in various services in order to serve natural person credit unions and generate revenue – I do not believe a payment system would be profitable in and of itself.
- 3) Should a separate charter be available for corporates that want to provide investment services?
 - I do not see a need for that action.
- 4) Should NCUA establish a legal and operational firewall between payment system services and other services?
 - I do believe a firewall would be a prudent defense against the situation we find ourselves in



today, but not by isolating the payment system from other services. My thought would be to place the “firewall” between the investment side of the equation from the remainder of services offered by our corporates.

- 5) Are there sufficient earnings potential in offering payment systems to support a limited business model that is restricted to payment services only?
 - Without knowing the specifics of each corporates business model, it would be impossible to answer that question with certainty; however, I do believe that isolating the investment operation from the processing side would be viable. Increase in the fee structure could result in higher fees for npcu.

Liquidity and Liquidity Management

Corporate credit unions are an important source of liquidity to credit unions and we are of the opinion that recent events have shown a weakness in the corporate system with regard to their own cash flow needs.

- 1) Should liquidity be considered a core service of the corporate system? If so, what steps should be taken, and by whom, to preserve and defend the liquidity function?
 - Most definitely, liquidity from corporates is a critical factor in small to mid-size credit unions that may not have the options of the larger credit unions, such as the Federal Home Loan Bank, etc. While these are unprecedented times, any restructuring of the corporates should include a permanent extension of the federal guarantee of deposits for natural person credit unions that is funded by the corporates themselves – just as we are required to fund our members share guarantee. I also believe corporates should have access to the Central Liquidity Fund (CLF) for their specific needs.
- 2) Should NCUA consider limiting a corporates ability to offer other specific types of products and services in order to preserve and defend the liquidity function?
 - Definitely not – liquidity is but one small piece of the services corporates have successfully offered to their natural person credit unions for years.
- 3) What specific types of products and services should corporates be authorized to provide?
 - Corporates should be able to offer any service needed by a natural person credit union as long as its viability is tested, a source of revenue is detected, and it complies with all rules and regulations.

Field of Membership

You have indicated that NCUA is contemplating whether or not its decision to allow corporates to have national fields of membership (FOMs) may have resulted in unforeseen risk taking. Without a doubt – the same can be seen in natural person credit unions.

- 1) Should NCUA return to defined FOMs, for example, state or regional FOMs?
 - I see no reason to restructure the corporates FOMs. While I stand by my statement above concerning the increased risk-taking, I do not think that the corporates’ FOMs were the determining factor in the situation we find ourselves in today.



Expanded Investment Authority

Corporates that meet certain criteria can currently qualify for expanded investment authority; such as the authority to purchase investments with relatively lower credit ratings than otherwise permissible under the rule.

- 1) Does the need for expanded authorities continue to exist? If so, should NCUA modify the procedures and qualifications, such as higher capital requirements? If so, what should the new standards be?
 - The expanded investment authority should be maintained, but with more oversight and restrictions that reduce the risk profile of the wholesale corporate portfolio. As with policies that natural credit unions must follow, investment restrictions should require thorough and regular credit analysis, concentration limitations, and be compelled to list prohibited risky investments. A higher capital requirement is a given evidenced by the situation we find ourselves in today.
- 2) Should any of the limits in existing expanded authorities be reduced or increased? If so, which ones? Once granted, should NCUA required periodic requalification for expanded authorities? If so, what should the timeframe be?
 - NCUA would be in a better position to determine the quantity of expanded authorities based on the wholesale corporate and then be prepared to back that decision. NCUA should consider a requirement for requalification with each examination or more frequently if deemed necessary.

Structure; Two-Tiered System

NCUA is soliciting comment on whether the current two-tier corporate system in its current form meets the needs of natural person credit unions.

- 1) Specifically, is there a need for a wholesale corporate credit union? If so, what should be its primary role?
 - Most if not all corporate credit unions utilize the services of the wholesale corporate as an integral part of their business model. The wholesale corporate should be a source of liquidity and investment opportunities for other corporates. One suggestion might be to allow only the wholesale corporate to invest in the more risky investments thereby managing one central portfolio making it easier to monitor and regulate.
- 2) Should there be a differentiation in powers and authorities?
 - Yes, the wholesale and retail environments are different – a differentiation in powers and authorities would be a necessity.
- 3) Does the current configuration result in an inappropriate transfer of risk from the retail corporates to the wholesale corporate?
 - It is my opinion that the risk at this point rests on the shoulders of ALL corporates and the structure that governs them.
- 4) Assuming the two-tiered system is retained, should capital requirements and risk measurement criteria (e.g., net asset value volatility), as well as the range of permissible investments, for the wholesale corporate be different from those requirements that apply to a retail corporate?
 - Most definitely and for the reasons stated above!



Corporate Capital

Core Capital

NCUA is considering revising certain definitions and standards for determining appropriate capital requirements for corporates.

- 1) Should NCUA establish a new capital ratio for corporates consisting only of core capital, and if so, what would be an appropriate level?
 - The capital of our corporate systems must be risk-based. A risk-based capital system would allow NCUA, corporates, and credit unions to view a corporates capital strength using the same rating system as agencies and counterparties. Each corporate should be required to maintain a capital level of at least 4% ranging up from that based on the risk of their balance sheet. If that capital level falls below their assigned level, they should provide NCUA and the Board of Directors a plan to restore the capital back above the required limit in 24 months.
- 2) What actions are necessary to enable corporates to attain a sufficient capital ratio as described above.
 - I believe their capital should be the result of earnings and not paid-in capital by natural person credit unions.
- 3) What should be an appropriate timeframe for corporates to attain a sufficient capital ratio as described above.
 - In order to accomplish this, they should be given a window that coincides with TCCUSGP – whatever that turns out to be.
- 4) How much emphasis should be placed on generating capital through undivided earnings?
 - As stated above, I believe the corporates' capital should come from their earnings as do natural person credit unions. I am not a proponent of paid in capital.
- 5) Should a corporate be required to limit its services only to members maintaining capital with the corporate?
 - No I do not believe they should be limited, but as stated above, I am not in favor of paid in capital – instead they should be able to compete for business based on the quality of the services they offer. Survival of the fittest so they say.

Membership Capital

NCUA is considering whether they should continue to allow membership capital in its current configuration, or should they eliminate or modify certain features, such as the adjustment feature, so that membership capital meets the traditionally accepted definition of two-tier capital.

- 1) Should NCUA continue to allow membership capital in its current configuration, or should it eliminate or modify certain features, such as the adjustment feature, so that membership capital meets the traditionally accepted definition of two-tier capital?
 - Until such time as the corporate can build its capital to the desired level, the membership capital should remain in place. Once achieved, the capital deposit should be returned to the natural person credit union.
- 2) Should the adjusted balance requirements, currently in §704.3(b)(3), be tied only to assets, and should limits be imposed on the frequency of adjustments?
 - Yes while in existence the balance requirements should be tied to assets with a frequency of



one year.

- 3) Should there be a requirement that any attempted reduction in member capital based on downward adjustment automatically result in the account being placed on notice, within the meaning of §704.3(b)(3), so that only delayed payout after the three-year notice expires is permissible?
 - Such a requirement is not justified in my opinion.
- 4) Should there be a requirement that any withdrawal of membership capital be conditioned on the corporates ability to meet all applicable capital requirements following withdrawal?
 - Not after their capital ratio is met through earnings.

Risk-Based Capital and Contributed Capital Requirements

NCUA is questioning whether or not capital in the corporate credit unions should remain as a two-tiered system.

- 1) Should NCUA consider risk-based capital for corporates consistent with that currently required of other federally regulated financial institutions?
 - Most definitely!
- 2) What regulatory and statutory changes, if any, would be required to effectuate such a change?
 - The corporates should be required to follow the same stress test and ALM modeling that is required of natural person credit unions. New guidelines should focus on the process that must be followed to ensure proper due diligence and regular credit monitoring by the corporates.
- 3) Should a natural person credit union be required to maintain a contributed capital account with its corporate as a prerequisite to obtaining its services?
 - No I do not believe they should be limited, but as stated above, I am not in favor of paid in capital – instead they should be able to compete for business based on the quality of the services they offer. Competition makes us strong!
- 4) Should contributed capital be calculated as a function of share balances maintained with the corporate? What about using asset size?
 - As stated above, I am not a proponent of continuing the contributed capital environment in the corporates.

Permissible Investments

Permissible Investments

Corporates currently have the authority to purchase and hold investments that would not be permissible for natural person credit unions. Thus, natural person credit unions are indirectly exposed to any risky investments held by the respective corporate.

- 1) Should corporate investment authorities be limited to only those investments allowed for natural person credit unions?
 - No. Corporates must be able to invest in products not allowed by natural person credit unions in order to earn a spread and provide a return that will allow the cessation of contributed capital.
- 2) Should certain categories or specific investments be prohibited? (For example, collateralized debt obligations, net interest margin securities, and subprime and Alt-A asset-backed securities.)



- No. Corporates should be allowed to invest in any securities allowed under current regulation – however, they should have adequate capital in order to do so.

Credit Risk Management

With many questioning the reliability of credit ratings for investments, NCUA is considering limiting the extent to which a corporate may focus on rating provided by Nationally Recognized Statistical Rating Organizations (NRSROs).

- 1) Should NCUA require more than one rating for an investment, or require that the lowest rating meet the minimum rating requirements of Part 704?
 - In light of the situation we find ourselves in today, I think that approach would be prudent.
- 2) Should additional stress modeling tools be required in the regulation to enhance credit risk management?
 - As above, anything to protect the natural person credit unions from the situation we find ourselves in today should be explored.
- 3) Should Part 704 be revised to provide specific concentration limits, including sector and obligor limits? Is so, what specific limits would be appropriate for corporates?
 - Yes. One of the major contributing factors in our current situation is the lack of concentration levels. Any new enhancements should definitely address proper limits and controls in this area.
- 4) Should corporates be required to obtain independent evaluations of credit risk in their investment portfolios?
 - Yes. Although the recent dismal reporting by the major rating agencies is problematic, they possess analytical resources that corporates cannot realistically duplicate.
- 5) Should corporates be required to test sensitivities to credit spread widening?
 - Most definitely, why should they not be held to the same standards as natural person credit union?

Asset Liability Management

NCUA is considering reinstating the requirement that corporates perform net interest income modeling and stress testing. Alternatively, NCUA may consider some form of mandatory modeling and testing of credit spread increases.

- 1) Should NCUA require corporates to use monitoring tools to identify these types of trends? What, if any, tangible benefits would flow from these types of modeling requirements?
 - Yes NCUA should reinstate NII modeling and stress testing. In doing so, it would give the corporate credit unions and NCUA a better understanding as to the true performance of the investment portfolio.

Corporate Governance

Due to the sophistication and far-reaching impact of corporate activities, NCUA is considering several changes to corporate boards.

- 1) Should NCUA establish minimum standards for directors in regard to their level of experience and independence?



- Currently, corporate boards are manned by management and officials of natural person credit unions. NCUA should require director qualifications and training requirements. We are in favor of independent, compensated individuals sitting on corporate boards.
- 2) Should NCUA impose term limits on corporate directors, and if so, what should the maximum term be?
- Term limits are appropriate as long as they are not too restrictive thereby leading to inexperienced and unsophisticated board members. The term limit should be set by the individual corporates and their membership.
- 3) Should corporate directors be compensated?
- No. It is our opinion that compensating board members goes against the core credit union philosophy.

I would like to thank NCUA for the opportunity to participate and provide our comments on this critical issue. We are dependent on the corporate system and believe in their longevity, however, do feel that they should be held to a tighter scrutiny than they have experienced in the past. Your Board faces unparalleled challenges and our hope is the final result will be the same for all – restore trust in the corporate system.

Sincerely,

Cheryl Gibson
President